No. 266

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1943

CENTRAL-ILLINOIS SECURITIES CORPORATION and CHRISTIAN A. JOHNSON

v.

SECURITIES AND EXCHANGE COMMISSION, THOMAS W. STREETER, et al., THE HOME INSURANCE CO., et al.

## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Central-Illinois Securities Corporation and Christian A. Johnson pray that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Third Circuit entered on March 19, 1948 vacating a decree of the United States District Court for the District of Delaware entered May 29, 1947, with the direction to enter an order disapproving in part a plan under Section 11(e) of the Public Utility Holding Company Act as not being fair and equitable within the purview of Section 11(e) of said Act and to return the record to the Securities and Exchange Commission to the end that it may take such action as the facts and the law may require.

Petitioners are respondents with respect to three petitions for certiorari which have been filed by the respondents named herein to review the same judgment (Nos. 226, 227, 243), and petitioners will file a timely brief in opposition to said petitions. The certified transcript of the record and the requisite number of copies of the printed record have been furnished in accordance with paragraphs 1 and 7 of this Court's Rule 38, having been heretofore filed by the Securities and Exchange Commission in No. 226 on behalf of all the parties pursuant to stipulation of counsel (R. 41).

## Opinions Below

The opinion and judgment of the Court below (R. 12) and the opinion denying petitions and cross-petitions for rehearings (R. [illegible]) are reported at 168 F. 2d 722. The opinion of the District Court is reported at 71 F. Supp. 797 (R. 283a), but its detailed Findings of Fact and Conclusions of Law (R. 293a-317a) are not reported. The Findings and Opinion of the Commission dated December 4, 1946 and January 8, 1947 have not yet been officially reported but are set forth in the Commission's Holding Company Act Releases Nos. 7041 (R. 25a) and 7119 (R. 128a).

## Jurisdiction

The judgment of the Circuit Court of Appeals for the Third Circuit was entered March 19, 1948, and its judgment denying petitions and cross-petitions for rehearing was entered June 11, 1948. The jurisdiction of this Court is invoked under Section 240 of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. 347), made applicable by Section 25 of the Public Utility Holding Company Act of 1935, 49 Stat. 803 (15 U. S. C. 79 *et seq.*).

## Statute Involved

Section 11(e) of the Public Utility Holding Company Act of 1935 provides as follows:

> "(e) In accordance with such rules and regulations or order as the Commission may deem necessary or appropriate in the public interest or for the protection of investors or consumers, any registered holding company or any subsidiary company of a registered holding company may, at any time after January 1, 1936, submit a plan to the Commission for the divestment of control, securities, or other assets, or for other action by such company or any subsidiary company thereof for the purpose of enabling such company or any subsidiary company thereof to comply with the provisions of subsection (b). If, after notice and opportunity for hearing, the Commission shall find such plan, as submitted or as modified, necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such plan, the Commission shall make an order approving such plan; and the Commission, at the request of the company, may apply to a court, in accordance with the provisions of subsection (f) of section 18, to enforce and carry out the terms and provisions of such plan. If, upon any such application, the court, after notice and opportunity for hearing, shall approve such plan as fair and equitable and as appropriate to effectuate the provisions of section 11, the court as a court of equity may, to such extent as it deems necessary for the purpose of carrying out the terms and provisions of such plan, take exclusive jurisdiction and possession of the company or companies and the assets thereof, wherever located; and the court shall have jurisdiction to appoint a trustee, and the court may constitute and appoint the Commission as sole trustee, to hold or administer, under the direction of the court and in accordance with the plan theretofore approved by the court and the Commission, the assets so possessed."

## Questions Presented

1. Did the Circuit Court properly order the vacating of the District Court's decree and the remand of the proceedings to the Securities and Exchange Commission where:

(a) The Commission had recognized that if the rationale on which it predicated an award of redemption premiums to preferred stockholders in a final liquidation under Section 11(e) of the Public Utility Holding Company Act were judicially determined to be invalid, that payment to the preferred stockholders of $100 per share plus dividends would be "fair and equitable"; and had entered an order alternatively approving such amount if the District Court found (as it did) payment of the premiums unfair and inequitable, and its determination were either not appealed or were affirmed upon appeal;

(b) The Commission had urged the District Court not to remand the proceedings to it by reason of finding the provision for payment of the premiums unfair and inequitable, but instead to enter its decree approving and enforcing the remainder of the plan and to authorize establishment of an escrow fund for the premium payments, pending appellate review of the District Court's determination respecting such premiums, which determination the Circuit Court affirmed;

(c) On the facts and the law as found by the District Court and affirmed by the Circuit Court, and further on the basis of supervening changes in applicable money rates, no amounts can be found payable to the preferred stockholders in addition to the $100 per share plus dividends already received, without violating the "fair and equitable" standard of Section 11(e);

(d) Remand of the proceedings to the Commission will result in substantial further expense and will seriously delay the distribution of approximately $4,000,000 to the common stockholders who have made large sacrifices in order to effect the complete liquidation of their enterprise in obedience to the requirements of the Public Utility Holding Company Act?

2. Does the Statute authorize, and the Fifth Amendment of the Constitution permit, applicable corporate charter provisions to be overridden where not reasonably necessary to effectuation of the Congressional objectives embodied in the Statute?

## Statement

These proceedings relate to a plan of liquidation filed with the Securities and Exchange Commission by Engineers Public Service Company ("Engineers"), in order to effect final compliance with a series of mandatory orders previously issued against Engineers by the Commission under Section 11(b)(1) of the Public Utility Holding Company Act of 1935 ("the Act"). The cumulative net effect of these Section 11(b)(1) orders, when taken in combination with the provisions of Section 11(b)(2) of the Act, was to require the complete and final dissolution of Engineers and its entire holding company system (R. 47a-48a, 139a-140a). The Engineers system, which at the time of the passage of the Act had comprised some seventeen electric, gas and other utility and non-utility companies throughout the United States, had been whittled down to only three operating companies in the course of Engineers' compliance with the Commission's mandatory divestment orders; and Engineers was required by outstanding Commission divestment orders to dispose of two of these remaining three.

When the dissolution plan was filed Engineers' capital structure consisted of common stock and preferred stock, the latter all having a stated book value of $100 per share (increased in 1938 from $96 per share, R. 301a) but being divided into three series carrying different dividend rates ($5, $5.50 and $6), and all being entitled in the event of "liquidation, dissolution, winding up" or any "reduction of its capital stock resulting in any distribution of its assets to stockholders", to $100 per share plus accrued dividends in preference to any payments to the holders of the common stock. However, if such liquidating acts were "voluntary", the preferred holders would in addition be entitled to the redemption premiums of each series (i.e., $5 per share for the $5 series, and $10 for the others). Under the provisions of the charter, the preferred stocks were callable at any time at the option of the company upon payment of these redemption amounts (R. 1403a-1431a).

Engineers' plan, so far as here material, provided in substance: (1) that the common stockholders of Engineers should initially pay $22,000,000 in cash into Engineers' treasury by purchasing the stock of one of the three remaining subsidiaries; (2) that this money plus treasury cash on hand (representing the proceeds of other property sales and retained earnings) would be used to effect the retirement in cash of all the preferred stock of Engineers at the charter liquidation amount of $100 per share plus dividends to the date of payment; (3) that promptly thereafter, the remaining assets of Engineers would be distributed among the approximately 13,000 common stockholders of Engineers as a final liquidating dividend, and Engineers would be dissolved.

## Commission Decision

In its Findings and Opinion issued December 5, 1946, the Commission held that the dissolution of Engineers was an involuntary dissolution made necessary by the mandatory provisions of Section 11 of the Act (R. 48a, 139a-140a). Unlike the dissolution involved in *Otis & Co.* v. *S. E. C.*, 323 U. S. 642, Engineers' liquidation would effect the dissolution not only of the holding company, but the final and complete disintegration of the entire holding company system.

Despite its finding that the dissolution of Engineers and its system was not voluntary, the Commission nevertheless held that the company must pay the preferred stockholders the redemption premiums which the charter provided were payable only in the event of a voluntary liquidation or redemption. These premiums totalled $3,204,795 in excess of the amounts specified by the charter as payable to the preferred holders in the event of liquidation, dissolution, winding-up or reduction of the corporation's capital stock resulting in any distribution of its assets to stockholders."

In reaching this result, which was directly contrary to a long line of Commission and Court decisions,[1] the Commission's initial postulate was that *Otis & Co.* v. *S. E. C.*, *supra*, established the proposition that charter liquidation provisions were not controlling in any liquidations under the Holding Company Act, but were merely one factor to be taken into account.[2] For that reason, the

[1] See note 21, *infra*.

[2] The Commission made no attempt to compare the complete and definitive dissolution of the Engineers system with the pseudo-liquidation involved in the *Otis* case, despite the plain reliance in the majority opinion of this Court upon the Commission's emphatic argument that the liquidation there involved (relating as it did merely to the top layer of a multi-tiered holding company structure) left essentially unchanged a vast holding company enterprise (See Commission Brief filed with this Court in *Otis & Co.* v. *S. E. C.*, p. 78.)

Commission stated the liquidation provisions of Engineers' charter could not be regarded as "conclusive" in determining the rights of the stockholders (R. 61a-62a). It thereupon proceeded to disregard these charter provisions entirely.

The amount which the preferred stockholders must receive, the Commission held, was "the investment value of their stock on a going-concern basis", and as though no liquidation were taking place (R. 67a-68a). The Commission noted that two witnesses (Badger, a witness on behalf of certain preferred holders, and Barnes, president of Engineers) had testified that "if there were no Holding Company Act, or if the Act were to be repealed today" they believed Engineers' preferred stock would sell on the market at or about their redemption prices and would probably be called and redeemed by the company.[3] The Commission thereupon stated that it was "conceded" and "unchallenged" that "the preferred has an investment value at least equal to the respective redemption prices"; and it held that this was the amount they must be paid (R. 67a-68a).

No mention was made by the Commission of Barnes' repeated and emphatic testimony that such "values" merely reflected the inflated stock market prices current at that

[3] Barnes, one of the two witnesses referred to, pointed out that "if there were no Holding Company Act, or if the Act were to be repealed today" so that Engineers were not compelled to liquidate, it would, of course, take advantage of the current low money rates to replace its outstanding preferred stock with preferred stock carrying a much lower dividend rate, thereby benefiting the common stockholders substantially (R. 522a-525a, 633a). The Commission's opinion made no reference to this portion of Barnes' testimony.

moment,[4] and could by no means be deemed the "fair value" of the stock for any representative period of time in the light of its very poor past record and future uncertainties. Despite the fact that the amounts to which the Commission held the Engineers preferreds entitled were admittedly the maximum which could be awarded if the stock were the highest grade of "gilt-edge" security, no mention was made by the Commission of Badger's admission that the Engineers preferreds were not "high grade" but at best "medium grade" (R. 1133a, 1485a); nor of Barnes' testimony that on the basis of the criteria customarily employed by financial analysts they are "closer to a low-grade preferred" (R. 1133a, 1140a); nor of the evidence establishing that during the period the preferreds were outstanding they were accorded by the leading independent analysis an investment rating of only C**, defined as "Preferred stocks with erratic dividend records which can be expected to make payments only under favorable conditions" (R. 1844a-1845a).[5]

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[4] The testimony of Badger and Barnes was given at various times over the period December 1945 through February 1946, at which time stock market prices (including those of public utilities) stood at the highest point since 1931. Barnes warned "we are in a boom period", and stressed its temporary nature (R. 667a). The Federal Reserve Bank Index of utility stock prices which stood at 130 in June 1946 subsequently declined to 94 by the end of 1947, indicating an average decline of about 28% (cf. Federal Reserve Bulletin).

The Commission has itself referred to the period of Barnes' and Badger's testimony as "the peak of the post-war market", and has admitted that "investment values" computed on the basis of yields and market prices then prevailing have since been adversely affected to a substantial extent. (*The United Light and Railways Company-American Light & Traction Co.*, Holding Company Act Release No. 7951, Dec. 31, 1947.)

[5] In an earlier portion of its opinion, the Commission did summarize statistically evidence in the record establishing that the preferred stocks had been in arrears of dividends for several years and had sold for considerable periods of time as low as $10-$14 per share for all series, and that the overall market price through the entire period from the time of issuance to the date of the testimony

Although the Commission purported to be determining the value of the preferred stock "on a going-concern basis" and "as though no liquidation were taking place", it did not determine or even consider what would be the value of the preferred stock for any period of time in the future if the liquidation compelled by the statute actually were not to take place and the preferred were permitted to remain outstanding as part of a continuing enterprise or "going-concern". On the theory adopted by the Commission, this would have necessitated consideration not only of normal prospective earning power, such as is fundamental in valuation for reorganization purposes,[6] but also of the prospective yields applicable to preferred stocks having investment characteristics comparable to those of Engineers. For the very essence of Badger's "expert opinion" (which the Commission simply adopted) that the preferred stockholders were entitled to receive more than the par value of their stock was that the unprecedentedly low money rates prevailing at that time enhanced the market value these preferred stocks would have (absent the liquidation) to an amount at least

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was only $63-$67 per share for all series (R. 62a); but no reference was made to these factors at the point where the Commission discussed the so-called "investment values".

Similarly, although the Commission's computations showed that these preferreds were actually a speculative *junior security* (being junior to 66.2% of the system's capitalization, R. 64a), no allusion to the significance of this factor is to be found anywhere in the opinion; nor is allusion made to the significance of the slim coverage for charges and dividends over the past decade (R. 64a) nor of the fact that for several years continuously charges and dividends had not been fully earned.

These omissions are all the more inexplicable in view of the fact that in the long line of decisions in which the Commission theretofore had refused to approve payment of premiums upon retirement of senior securities, it had repeatedly stressed all of these very factors. (See decisions cited n. 21, *infra*.)

[6] Cf. *Consolidated Rock Products Co.* v. *Dubois*, 312 U. S. 510, 526; *Group of Institutional Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, 565-6.

equal to their redemption prices.[7] Further, while allegedly determining values "ex the Act" ("apart from the impact of liquidation compelled by the Act"), neither the Commission nor Badger made allowance for the many important factors which came into existence directly as the result of this very statutory requirement for liquidation.[8] None of the other drastic impacts of the Act upon the common stockholders received consideration; nor did the Commission attempt to "find" the so-called "investment value" or any other value of the common stock on "a going-concern basis" ("apart from the necessity for liquidation") or otherwise.

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[7] Thus, Badger stated: "Except insofar as a preferred stock may be callable at a specific price, preferred stocks are in the nature of perpetual annuities; and should be valued by capitalizing their dividend rates at rates of capitalization which give full weight to inherent investment risk and money rates at the date of valuation" (R. 2062a). With respect to the then prevailing money rates (which he employed without modification in "valuing" the Engineers preferreds) he testified "* * * yields on preferred stocks are at the present time, the lowest which they have been in the history of our country, or, conversely * * * the prices of such stocks are at the highest levels ever experienced. The permanency of this situation will depend on the permanency of low interest rates" (R. 2065a). Several months from the time this testimony was given (and many months prior to the issuance of the Commission's findings and opinion) money rates and preferred stock yields commenced the sharp upward climb, and preferred stock prices the concomitant decline, which has been in progress ever since (see District Court Finding No. 52, R. 314a, and R. 122).

[8] For example, no allowance was made for approximately $24,500,000 which had accrued to the equity of the common stockholders of Engineers and which had been withheld from them largely because of the necessity of providing for this very liquidation (R. 306a, 469a-471a, 1395a). Instead this entire amount (equivalent to 60% of the preferreds' stated value) was credited to the preferred in determining its so-called "investment value *ex* the Act" (R. 306a, 312a).

## The District Court's Decision

After consideration of extensive oral argument and briefs by counsel for the Commission and all the other parties,[9] the District Court (to which the Commission had applied pursuant to Section 11(e) for entry of a decree approving and enforcing the plan) held that the provision of the amended plan for the payment of the amounts in excess of $100 per share (the premiums) was not consonant with the "fair and equitable" standard of Section 11(e), but that in all other respects the plan met the statutory requirements. The Court thereupon followed the course strongly urged by the Commission's attorneys,[10] of not remanding the proceedings to the Commission, but instead of approving and enforcing the plan except as to the premium payments, and requiring the latter to be deposited in an escrow fund approved by the Commission pending review of the District Court's determination. The Commission's opinions had expressly advocated this course (R. 75a, 136a), and its order of February 11, 1948 (R. 165a), had provided formal advance approval for it.

The disagreement of the District Court with the Commission as to the premium payments was basically a disagreement as to applicable legal principles. The Court regarded as erroneous and devoid of judicial support the Commission's thesis that the rights of security holders of a holding company enterprise which is being entirely and definitively liquidated pursuant to governmental edict should

[9] The company refrained from taking a position on the premium issue either before the District Court or the Circuit Court on the theory that it was in essence "a neutral stakeholder" in a controversy between its stockholders (R. 200a). Two groups of common stockholders (including petitioners) who had given timely and detailed notification to the Commission of their opposition to this phase of the plan (R. 135a, 2150a) independently presented their objections to the Court.

[10] R. 257a-261, 281a-282a.

be approached on the purely fictional hypothesis that "the enterprise continues", and the claims of the preferred holders (but not the common) measured "on a going concern basis", and "as though there were no Holding Company Act or as if the Act were to be repealed today" (R. 292a, 314a, 315a-316a).[11] The District Court was of the view that this recently evolved and mis-named "investment value" doctrine, as sought to be applied by the Commission in the case at bar, contravened firmly rooted decisions of at least four circuit courts of appeal and many district courts, as well as a long line of decisions of the Commission itself (R. 288a, 292a). These decisions uniformly hold that where retirement of senior securities is not the result of voluntary action by management of the junior security holders, but is mandatory by virtue of Section 11 of the Act, the equity holders must not be penalized by being made to pay premiums to the senior security holders as though a "call or redemption" were being effected on a normal "going-concern" basis.[12]

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[11] It may be noted that the District Judge (Judge Leahy) had been the first court to pass upon and approve the United Light plan subsequently upheld by this Court in *Otis & Co.* v. *S. E. C.*, 323 U. S. 624, the decision relied upon in the instant case by the Commission as support for the proposition here rejected by the District Court. Judge Leahy's cogent understanding of the issues involved in the *Otis* case is attested by his decision therein (51 F. Supp. 217, D. Del. 1943). Similarly, Judge Biggs, who wrote the Circuit Court's opinion in the instant case, was also the author of that Court's opinion in the *Otis* case (*In re Securities and Exchange Commission* (*Otis & Co.*), 142 F. 2d 411, C. C. A. 3, 1943).

[12] Decisions cited at n. 21, *infra*. Judge Leahy had himself repeatedly and uniformly upheld the Commission's determination that such premiums were not payable, although envisaging that a contrary view might possibly be justified upon proof of "a different fact situation" (*In re North Continent Utilities Corp.*, 54 F. Supp. 527, D. Del.). As the Circuit Court had occasion to point out (R. 30, 39) Judge Leahy, commencing with the earliest enforcement cases under the Act and continuously ever since, has had exceptionally specialized experience with Section 11(e) reorganizations, the Commission having applied to him for approval and enforcement of almost 50% of all Section 11(e) plans which have been brought to the Courts for enforcement.

Upon examination of the record which had been filed by the Commission with the Court, the District Judge ascertained a number of factors of which the Commission's opinion gave little or no inkling and which he found strongly corroborative of his view that payment of the premiums to the preferred would result in unfairness and inequity in a "colloquial" sense, as well as in its technical statutory sense; that Badger's "values" were largely "market" values (R. 310a) admittedly dependent upon continuance of governmental "pegging operations" designed to hold money rates to the artificially low level considered desirable because of the exigencies of governmental war financing (R. 313a-314a); that on the basis of the inherent investment qualities of the stocks, they were admittedly not "high grade" but rather "*medium* medium grade" or "low grade" (R. 311a); that even such inherent value as they possessed was in large measure due to the more than $24,000,000 of earnings which the common stockholders had, from the time enactment of the Holding Company Act sealed the company's doom, left in the enterprise to provide for its final liquidation (R. 306a); that the company had sustained heavy losses and sacrifices in carrying out the Commission's Section 11(b)(1) divestment orders, and that such losses had fallen and would necessarily fall on the common stockholders (R. 307a-308a); that the common stockholders had gone without dividends or return of any kind for 15 years while the preferred stockholders received full payment of their dividends over the entire period, aggregating approximately $90 per share (R. 302a, 306a); that in order to pay the preferred holders their full liquidating claim in cash the common stockholders would be required in connection with the liquidation to contribute an additional $22,000,000 cash, and to "mortgage" the assets distributable in the liquidation by advance payment of dividends (R. 308a-310a); that the common stockholders like the preferred stockholders were forced to relinquish continuance of the holding company enterprise in which they had invested (R. 311a, 312a, 316a).

The Court summed up its conclusions by formally finding that the enterprise in which the preferred and common stockholders of Engineers had invested had been frustrated and terminated by governmental action (R. 316a); that there was no valid basis for hypothesizing a "continuing enterprise" or "going concern" (R. 292a, 316a); that the Commission's "investment value ex the Act" doctrine as applied in this case was not only unsound and unrealistic in theory but inequitable and erroneous in application (R. 292a, 316a-317a). It held in the light of its "careful examination of all the relevant factors" that payment to the holders of the preferred stocks of Engineers of any amounts in excess of $100 per share plus accrued dividends would not be warranted or justified; would be unfair and inequitable to the holders of Engineers' common stock; and would contravene the fair and equitable standards of Section 11(e) of the Act (R. 317a).[13]

## The Circuit Court's Decision [14]

The Circuit Court rejected the Commission's contention that the District Court under Section 11(e) should be

[13] The District Judge stated that he found it unnecessary to conclude whether the charter liquidation provisions per se foreclosed any amounts in excess of $100 per share plus dividends, because "the conclusion is reached that the preferred stockholders are in any event not entitled to receive any such excess amounts on the basis of all the relevant considerations, even if the charter provision is not itself controlling. Said charter provision, however, if taken into account, constitutes an additional factor supporting the conclusions reached, as above stated" (R. 317a).

[14] Following the entry of the District Court's order, notice of appeal to the Third Circuit Court of Appeals was filed by the Commission and the two groups of preferred stockholders, one of which sought to stay consummation of any portion of the plan. The Commission joined in opposing the stay, which was denied in turn by the District Court, the Circuit Court and by Mr. Justice Burton of this Court. Thereupon, the escrow fund was duly established and the other provisions of the plan were consummated, including payment to the preferred stockholders of $100 per share and accrued dividends.

deemed a mere review court which must bow to the Commission's conclusions unless they wholly lack "any rational or statutory foundation" (R. 21, 34),[15] and held, after careful analysis of the statute and its legislative history, that a Section 11(e) Court must exercise its independent judgment as to the fairness and equity of a plan (R. 23, 33). It found that the District Judge treated the Commission's findings "as was proper * * * with respect" (R. 34), and commended his "careful and far-reaching examination of the relevant factors" (R. 34). It held that the Commission, in failing to take these important factors into account, had reached an inequitable and erroneous result (R. 38).

With respect to the Commission's attempted reliance on the *Otis* decision, the Circuit Court agreed with the District Court that the liquidation of the Engineers system was a complete and definitive termination of the enterprise, and thus differed materially from the mere simplification of a continuing holding company system involved in the *Otis* decisions (R. 36).[16] It held that even if it was permissible under these circumstances to measure security holders' rights on the fictional hypothesis of a "going concern" without regard to the liquidation which was in fact taking place under compulsion of the Act (i.e., "ex the Act"), the so-called "investment value" formula as applied by the Commission in this case to measure only the claims of the preferred holders "ex the Act" failed to produce that "equitable equivalence" for the rights of both classes

[15] The Court pointed out that the Commission's demand that Section 11(e) Courts should be relegated to the position of mere review Courts was at sharp variance with the positions which the Commission has for many years taken before the Courts and before Congress, wherein the independent plenary role of the District Court with respect to 11(e) plans was heavily emphasized (R. 30-31).

[16] As was pointed out *supra* (n. 11), Judge Biggs wrote the Third Circuit's opinion in the *Otis* case as well as in the case at bar.

of security holders which is of the very essence of the *Otis* rationale (R. 38).

The Third Circuit squarely affirmed the determination of the District Court that the provision of the plan for the payment of the premiums was unfair and inequitable (R. 39, 140). It also found "proper" and upheld the escrow arrangements embodied in the District Court's order (R. 40). Yet, notwithstanding its full approval of the District Court's reasoning and findings, the Circuit Court concluded that the District Court should have remanded the proceedings to the Commission.

On the question of remand, the Circuit Court's reasoning was in essence, that the disapproval by the District Court of the provision for payment of the premiums effected an "amendment" in the plan which under the Statute must receive the Commission's approval as well as of that of Court (R. 39). In addition, the Circuit Court's opinion suggests that the District Judge engaged in a species of "valuation" in formally finding that payment to the preferred holders of $100 per share plus dividends would be fair and equitable to the preferred and that payment of any additional amounts would contravene the "fair and equitable standard" of Section 11(e), instead of merely holding the premium payments as proposed in the plan unfair and inequitable and remanding the plan to the Commission. Stating that "The problem is and will remain until its disposition by the Commission, one of valuation of the securities of Engineers, viz., the preferreds and the common" (R. 40), the Court vacated the decree of the District Court [17] and remanded the proceedings to it:

> "with directions to enter an order disapproving the plan as not being fair and equitable within the purview

[17] It is clear that the Court intended to vacate only so much of the District Court's decree as related to the premium payments since the remainder of the plan had already been fully consummated; presumably this will be more precisely stated when the Court's mandate is ultimately issued.

of Section 11(e) of the Public Utility Holding Company Act, and to return the record to the Commission to the end that it may take such action as the facts and the law may require" (R. 40, 41).

Petitions for rehearing were filed by the appellants in the Circuit Court with respect to the Court's affirmance of the determination that the proposed payment of the premiums was unfair and inequitable. Answers thereto and cross-petitions were filed by the appellees (including petitioners) with respect to the requirement for remand to the Commission (R. 97). The Court denied the petitions and cross-petitions, stating in a short opinion its adherence to the views previously enunciated (R. 138).

## Reasons Relied On for Allowance of the Writ

The decision of the Circuit Court that these proceedings must be remanded to the Commission for further action raises substantial issues in the administration of the Public Utility Holding Company Act and with respect to the impact of the Act upon the many thousands of security holders of holding companies which are required by the Act to terminate their existence. Issuance of this writ is especially vital if the Court is disposed to grant the petitions heretofore filed by respondents (Nos. 226, 227, 243) in order that the Court may have full latitude to consider and dispose of all the important questions arising from the judgment to be reviewed. Further, it is believed the Circuit Court's requirement for remand of these proceedings to the Commission conflicts with principles enunciated by this Court in other reorganization cases, and presents issues which have both procedural and substantive aspects of importance.

## I. Procedural Aspects

(1) The Circuit Court's decision requiring remand negates a sound and essential procedure for coordinating and dovetailing the overlapping statutory roles of the Securities and Exchange Commission and the district courts in approving and effectuating reorganization and liquidation plans under Section 11(e) of the Act. Many plans presented to the district courts involve no controversial questions, and thus ordinarily receive swift approval from the court on the basis of the Commission's findings and opinion. But where, as here, sharp issues are raised bearing on the fairness of the plan to a class of security holders, the Circuit Court recognized and vigorously affirmed that the district court may not enter its decree approving and enforcing a plan merely because "the Commission's conclusions are not wholly lacking in a rational or statutory foundation" (as the Commission and the other appellants before the Circuit Court contended), but must exercise an independent and carefully considered judgment as to whether the plan satisfies the statutory requirement of "fairness and equity" to the persons affected (R. 33.)[18] Concurring as we do in the foregoing view of the respective duties of the Commission and the District Court, we believe the Circuit Court thereafter reached an erroneous and untenable result in concluding that the Commission could not, or that in this instance it did not, give advance approval to an alternative treatment of the preferred stockholders by payment of $100 per share and accrued dividends contingent upon determination by the District Court (subject to appellate review) that payment of the premiums was not fair and

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[18] Cf. *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, 479:

> "For example, there may arise controversies over the priority or the validity of claims. A Commission finding involving such problems would require an independent examination and an affirmation by the Court." Cf. *Comstock* v. *Group of Investors*, 68 S. Ct. 1454, 1462.

equitable. The Circuit Court's statement that the statutory requirement for approval of a plan by both the Commission and the District Court may not be "waived" or "rejected" (R. 139) is not to be gainsaid, but this does not mean that the Commission may not foresee the possibility that the courts may reach a contrary conclusion to that of the Commission with respect to one or more phases of the plan, and that the Commission may not provide in advance for its concurrence within specified limits with such judicial determination, especially where it relates to questions which do not go to the heart of the plan. Indeed, it is our view that this is virtually the only sound and rational procedure, within the statutory framework as correctly interpreted by the Circuit Court, for dovetailing the dual functions of the Commission and the courts without interminable delays resulting from shuffling proceedings back and forth from one to the other.[19] This view is supported by, and the Circuit Court's requirement for remand conflicts with, expressions of this Court with regard to the somewhat (though not entirely) analogous roles of the district courts and the Interstate Commerce Commission relative to railroad reorganization under Section 77(e) of the Bankruptcy Act. Thus, in *Ecker* v. *Western Pacific R. R. Co.*, 318 U. S. 448, the Court stated (p. 475): "These reorganizations may be attained only through properly coordinated action between the Commission and the Court"; and admonitions of like import bear-

[19] Respondents have persistently urged, on the other hand, that these functions should be accommodated merely by requiring the District Court to bow to the Commission's judgment unless it "wholly lacks any rational and statutory foundation". We think it is clear that not even this draconian standard of review could save the Commission's decision in the instant case. But in any event the Circuit Court's conclusion that accommodation on this basis cannot be achieved without violation of the clear statutory language and intent is plainly unassailable in the light of its careful reasoning and statutory analysis.

ing on the need for expediting reorganizations of this character have been repeatedly put forth by the Court.[20]

(2) The Commission, in requiring the plan to be amended to propose payment of the premiums over the objections of the company and the common stockholders, was necessarily aware that there existed no judicial sanction whatever for such premium payments, and that to the contrary the Commission itself and numerous Courts, including four different Circuit Courts of Appeals, had consistently and uniformly held over a period of five years that payment of premiums to senior security holders at the expense of the junior holders could not be required in reorganizations or liquidations under Section 11(e) of the Act in consonance with the fair and equitable standard of Section 11(e).[21]

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[20] See also *Continental Illinois Bank* v. *C. R. I. & P. Ry. Co.*, 294 U. S. 648, where the Court stated (p. 685):

> "Not only are those who institute the proceeding and those who carry it forward bound to exercise the highest degree of diligence, but it is the duty of the Court and of the Interstate Commerce Commission to see that they do. Proceedings of this character, involving public and private interests of such magnitude should, so far as practicable, be given the right of way both by the Court and by the Commission to the end that they may be speedily determined."

Cf. also *Insurance Group* v. *Denver & Rio Grande W. R. Co.*, 329 U. S. 607, 612; *Federal Trade Commission* v. *Curtis Co.*, 260 U. S. 568, 580; *International Shoe Company* v. *Federal Trade Commission*, 280 U. S. 234, 297.

[21] *New York Trust Co.* v. *S. E. C.*, 131 F. 2d 274 (C. C. A. 2d, 1942), *cert. den.* 318 U. S. 786, *rehearing den.* 319 U. S. 781; *City National Bank & Trust Co.* v. *S. E. C.*, 134 F. 2d 665 (C. C. A. 7, 1943); *Massachusetts Mutual Life Insurance Co.* v. *S. E. C.*, 134 F. 2d 665 (C. C. A. 7, 1943), *cert. den.* 327 U. S. 796; *In re Standard Gas & Electric Co.*, 151 F. 2d 326 (C. C. A. 3, 1945); cf. *Bailey* v. *Minsch*, 168 F. 2d 635 (C. C. A. 1, 1948).

In the District Courts, see *In re North Continent Utilities Corp.*, 54 F. Supp. 527 (D. Del., 1944); *In the Matter of Consolidated Electric & Gas Co.*, 55 F. Supp. 211 (D. Del., 1944); *In re Central States Power & Light Corp.*, 58 F. Supp. 877 (D. Del., 1944);

Under the foregoing circumstances, it would have required a singularly myopic vision (or perhaps an overweening confidence in judicial deference to the Commission's new views) for the Commission not to foresee at least the possibility that the provision for payment of the premiums might be found unfair and inequitable by the courts; and would obviously have been an act of administrative irresponsibility if the Commission did not make appropriat provision for this contingency in order to avoid the necessity for remand to the Commission and subsequent resubmission to the Courts, especially since the question was of relatively narrow scope and in no way touched the heart of the plan. Both the Commission's opinions (R. 75a, 136a) and its amendatory order of February 11, 1947 (R. 165a-174a), were intended to, and did, make such provision by approving as fair and equitable payment to the preferred holders of the liquidating preference of $100 per share plus accrued dividends and such additional amounts, if any, not exceeding the aggregate premiums with interest thereon, as might be thereafter approved by the enforcement Court's order which had become final for lack of appeal or which had been affirmed on appeal. As the Commission has itself stated: "* * * the Commission has already contingently approved an alternative allocation of cash to preferred stockholders at the amount of the liquidation preference if as a result of the processes of review in the District Court and on appeal therefrom this should be judicially determined fair and equitable." [22]

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*In re Standard Gas & Electric Co.*, 59 F. Supp. 27 (D. Del., 1945); *In re Interstate Power Co.*, 71 F. Supp. 164 (D. Del., 1947); *In re Laclede Gas Light Co.*, 57 F. Supp. 997 (E. D. Mo., 1944).

With respect specifically to retirement of preferred stocks without premiums, see *Cities Service Power & Light Co.*, Holding Company Act Release No. 4944; *Georgia Power & Light Co.*, Holding Company Act Release No. 5568; *El Paso Electric Co.*, Holding Company Act Release No. 5499.

[22] R. 44, note 1, Commission's petition for rehearing in the Circuit Court.

It is thus apparent that the Commission had given its prior consideration and advance approval to the plan in the form approved and enforced by the District Court's order of May 29, 1947 (R. 318a); and indeed the record discloses that this order was actually drafted and submitted to the District Court for signature by the Commission's attorneys (R. 357a). These circumstances scarcely justify the Circuit Court's statement that the District Court erred in entering an order approving and enforcing the plan as amended *by it*,[23] and without the Commission's prior consideration and approval. On the contrary, the procedure followed by the District Court in every particular was that which the Commission in its opinions and orders and by its attorneys in open court,[24] requested and urged the Court to follow, including establishment of the escrow fund and non-remand of the proceedings to the Commission by reason of the Court's disapproval of the premium payments. Even the very language of the escrow agreement embodied in the Court's decree, as well as the decree itself as has been stated, were formulated and submitted to the Court by the Commission's attorneys. Although concededly these circumstances do not insulate the Court's decree from attack if the Commission's actions were in effect "*ultra vires*", we submit that they do completely refute any suggestion that the Court engaged in a process of amending the plan in respects which procedurally, at least, had not received the full concurrence and approval of the Commission, and, indeed, as to which

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[23] "The Court below, therefore, erred in one particular. *It entered an order approving and enforcing the plan as amended by it.* It was without power to do this. The provisions of Section 11(e) make it clear that the Commission in the first instance must approve the plan and find it to be fair and equitable. If, as here, the district court disagrees with the conclusion of the Commission that the plan is fair and equitable, it must refuse to approve the plan and 'remand' the record to the Commission for further and appropriate action by it" (R. 39; emphasis supplied).

[24] R. 257a-260a, 281a-282a.

the Commission had not actually been the prime mover. Nor do we think the procedure urged upon the Court by the Commission can properly be deemed "ultra vires". If the Courts did not find the Commission's new "investment ex the Act" doctrine consonant with established legal principles and the statutory intent, nothing further remained to be decided; for in such event the preferred holders necessarily must receive the liquidating preference of $100 per share plus dividends, in conformance with a long line of Commission and Court decisions. Accordingly, the Commission correctly recognized that the basic issue was one of legal and statutory interpretation, as to which the last word was not in the Commission but in the Courts.[25] Therefore, in approving as fair and equitable payment of the liquidation preference in the event the District Court held payment of the premiums unfair and inequitable (and such determination became final for lack of appeal or were affirmed upon appeal), it is evident the Commission was not "waiving" or "rejecting" its statutory role, but was performing it in the only way consonant with reason and the repeated admonitions of this Court for expeditious and coordinated procedure in reorganizations of this character.[26]

(3) A valid basis is also lacking for the Circuit Court's suggestion that the District Court may have substituted

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[25] If confirmation be needed for this proposition, it is amply furnished by the legislative history of the statute, to which reference was made in the Circuit Court's opinion (R. 23, 23). For example, Senator Wheeler (who had the Bill in charge in the Senate) stated during the debates:

> "* * * the provision does not oust the jurisdiction of the Court at all, because the Court has to approve the plan even though the Commission approves it. In other words, there is really a double-check upon the plan, *and final determination rests as in the past in the courts*" (79th Cong. Rec. 8845, 74th Cong., 1st Sess.; emphasis added).

[26] See note 20, *supra*. Cf. *Comstock* v. *Group of Investors*, 68 S. Ct. 1454; majority opinion p. 1462, minority p. 1467.

its "valuations" and "estimates" for those of the Commission (R. 39). In essence this seems to reduce itself to a contention that the District Judge should have worded only negatively what he also worded affirmatively; that he should have held the provision for premiums "unfair and inequitable" without also finding affirmatively that the preferred holders received "fair and equitable" treatment upon receipt of $100 per share plus dividends without the premiums.

What the District Court "valued" was not the preferred stocks, but the Commission's "investment value ex the Act" doctrine. The initial and basic issue before the Court was the legal validity of the Commission's new doctrine, and in rejecting this doctrine squarely on the merits as a matter of law,[27] the District Judge merely adverted (though searchingly) to numerous relevant factors which confirmed to his satisfaction as a court of equity that payment of the liquidation preference without premiums would produce a

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[27] Judge Leahy addressed himself to this doctrine as follows (R. 311a-312a):

"Analysis of the value of the Engineers preferreds on a 'going concern' basis is largely an exercise in semantics, since the Act dictates the dissolution of Engineers and of the entire holding company enterprise, and thus makes impossible the 'going concern' in which the preferred and common stockholders engaged to invest. If not for the requirements of the Act, Engineers as a 'going concern' would have been free to take advantage of the present low money markets by calling and redeeming its preferred stocks and replacing them with preferred stocks carrying a lower dividend rate than those now outstanding; it would thus continue to enjoy the leverage advantages of senior capital, but at a substantially lower cost. Under these circumstances, payment of the premiums to the preferred stockholders would have been consonant with the purposes and intent of the charter redemption provision. But the Act has made it impossible for the Company and the common stockholders to avail themselves of these benefits contemplated by the contract, along with the many other advantages which would have accrued to them as a 'going concern, exclusive of the impact of Section 11'."

result wholly fair and equitable in its realistic ("colloquial") sense as well as in the technical statutory sense.[28]

The Circuit Court squarely affirmed the District Court's determination, after reviewing and approving Judge Leahy's reasoning and his "careful and far-reaching examination of the relevant factors" (R. 34, 140). The Circuit Court should therefore have affirmed the District Court's decree, without requiring the remand.[29]

## II. Substantive Aspects

The Circuit Court's requirement for remand of the proceedings to the Commission, while couched largely in procedural terms, has undertones which raise substantive issues of far-reaching importance if interpreted as the Commission has already indicated it contemplates in the event of remand of the proceedings to it.[30] These substantive issues stem principally from the sentence near the end of the Circuit Court's opinion which states: "The problem is and will remain, until its disposition by the

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[28] To be sure, the Court also made clear in its findings that even assuming the validity of the Commission's basic doctrine it could not accept the Commission's thesis that "investment values" may properly be determined on the basis of market prices and money rates as of a given moment, without regard to past and future events of significance (Findings 41-54, R. 310a-315a). But here again the Court was not "valuing" stock but pointing to the fallacies in the Commission's formula.

[29] It may be observed that the Circuit Court's expressed hope that the delay might be "of short duration" (R. 139) hardly derives encouragement from the record to date. Engineers' plan was filed with the Commission September 10, 1945; the Commission's findings and opinion were issued December 4, 1946, and its supplemental opinion and order January 8, 1947 (R. 118a, 141a).

[30] In its petition for rehearing in the Circuit Court the Commission stated its understanding of the issue on remand as follows: "* * * to require a remand merely for the purpose of a Commission finding that what the common stockholders receive in the plan is at least equal to what they give up in the plan, *is to require a statement in different terms of what the Commission has already found*" (R. 53; emphasis added).

Commission, one of valuation of the securities of Engineers, viz., the preferreds and the common" (R. 40).

The suggestion that a problem of "valuation" remains for disposition is illusory when viewed together with the preceding portions of the Court's opinion which discuss the fallacies of the Commission's "investment ex the Act doctrine" (R. 36-38) and the "pertinent factors" and "substantial equities" (R. 38) which must be considered whether evaluation proceeds "intra the Act" or "ex the Act". For in the light of these factors (which are the very ones considered by the District Court) no process of "valuation" can produce a result different from the one arrived at by the District Court. Any one of these considerations and factors would present virtually an insuperable barrier to a determination that the preferred holders are entitled to more than the $100 per share plus dividends they have already received; and in combination they are absolutely fatal to any such determination.

If the rights of the stockholders are determined realistically in the light of the authentic and compulsory liquidation which has in fact taken place ("intra the Act") the amount already paid to the preferred stockholders marks the outer limit of the preferreds' claim whether the charter liquidation provisions be recognized as dispositive,[31] or a

[31] Although the District Court found it unnecessary to decide the question of whether the charter provisions are themselves "dispositive of the issue", considering them merely one factor supporting the conclusion that $100 per share plus dividends is fair and equitable (R. 287a, 317a), and the Circuit Court also did not deem them dispositive (R. 34), we continue to maintain that these charter provisions are in fact controlling in respect of the type of final liquidation which both courts found has here taken place. Not only does this create a vital distinction from the *Otis* case, as the Circuit Court held (R. 36), and not only does the Engineers' charter contain significantly different provisions from the charter considered in *Otis*, but that decision held only that the charter liquidation provisions were not "*matured*" or "*accelerated*" by virtue of that pseudo-liquidation compelled by the Act; it did not hold that the maximum amount specified in the charter as payable to the preferred in a liquidation may be *exceeded*.

We also continue to maintain that the overriding of these applicable charter provisions to subserve no purpose reasonably related

species of equitable rescission by operation of law is deemed to have occurred as a result of the governmental frustration of the enterprise,[32] or an overall "weighting" of the equities is made in order to arrive at a result which is fair and equitable in a non-technical ("colloquial") sense.[33] On the other hand, if the rights of the security holders are to be determined on a going-concern basis "apart from liquidation" ("ex the Act"), no amount in excess of $100 per share can be found for the preferred if there merely be restored to the credit of the common holders the more than $24,000,000 left by them in the enterprise to provide for the liquidation (R. 306a, 312a); or if account be taken of the other sacrifices and deprivations sustained by the common in carrying out the liquidation (R. 307a, 36-7); or if their claims be measured consistently with those of the preferred (as the Court held they must, R. 35-8) on a going-concern basis "ex the Act".

Indeed, to the extent that *investment value* is entitled to any weight under the rulings of the Courts below in determining the rights of the security holders in this liqui-

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to the Congressional objective in enacting Section 11 would violate vested rights of the common stockholders protected by the Fifth Amendment of the Constitution, a question which this Court expressly stated it did not reach in that decision (*Otis & Co.* v. *S. E. C.*, 323 U. S. 624, 640; but see dissenting opinion, pp. 645, 648-9).

[32] Cf. District Court Conclusions 2-8 (R. 316a). See also 6 *Williston on Contracts* (1938) 5486 (n. 139) where, in discussing judicial decisions with respect to governmental frustration, it is stated: "These decisions may profitably be compared with those where mutual mistake as to some vital characteristic of a thing contracted for has been held to justify rescission." Elements of this doctrine are also found in the premium decisions cited in n. 21, *supra*.

[33] This was virtually conceded by appellants in the Court below. For example, the Commission's Reply Brief (p. 3) stated: "* * * there are no considerations of colloquial equity upon which the Commission would rely as a basis for according an increased participation to the preferred stockholders."

dation; it alone (and wholly apart from all the other considerations already mentioned) forecloses a finding of more than $100 per share and dividends for the preferred. For the Commission did not and could not determine that these preferreds actually have an authentic, *investment value* in excess of $100 if this term be employed in its normal sense. What the Commission did was merely to credit and accept the testimony of Badger that as of the date of his testimony, these preferreds would have had a *market* value approximating the redemption prices if dissolution were not required by the Act. And Badger's opinion as to this hypothetical market value [34] was based not on the inherent investment qualities of these stocks (which the evidence established was at best a low-grade medium holding company preferred, R. 314a) but on the extremely low money rates and yields prevailing at that particular moment: "the lowest which they have ever been in the history of our country" and "conversely, the prices of such stocks [preferred] are at the highest levels ever experienced" (R. 2065a).

Both Courts below were struck by the Commission's anomalous and almost inexplicable [35] action in terming the momentary market value of the preferreds in May 1946 their "investment value" on a "going-concern" basis; [36] and held that if rights are to be measured on the Commission's fictional theory of "a going-concern", then values must also be determined on that basis (R. 312a-315a, 35-37). The

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[34] Even the actual market values were lower than the redemption prices on the date of Badger's testimony (R. 2062a).

[35] In other decisions the Commission has consistently rejected market values as a criterion for valuation in Section 11(e) plans. Cf. *Washington Railway and Electric Co.*, Holding Company Act Release No. 7410 (May 1947), where the Commission stated (p. 27): "However, we have never considered market values as determinative of the fairness of a Section 11(e) plan."

[36] District Court Findings 48-54 (R. 312a-315a); and see Circuit Court's statement regarding the District Court's "cogent finding" as to Badger's money rates (R. 19).

drastic decline in preferred stock yields and market prices which commenced shortly after Badger's testimony and has continued almost steadily since, adds further incontrovertible proof to the evidence pointed to by Barnes (and found by the District Court) which establishes that the Engineers preferreds have not in the past and cannot now be valued at more than $100 on a going-concern basis. Not only did the Circuit Court find that the evidence in the record bears this out,[37] but the Court was asked to take judicial notice of authoritative and competent data establishing that if the liquidation had not in fact taken place (as the Commission hypothesized) the Engineers preferreds would have a present market value of not more than $90-$95 per share (R. 122-3).

In the light of the foregoing factors, we believe it is evident that remand to the Commission can only lead to a finding by the Commission that in view of the holdings of the District and Circuit Courts, payment to the preferred holders of the amounts already received is fair and equitable, and that this is the "disposition by the Commission" contemplated in the Circuit Court's sentence previously quoted (*supra*, p. 27).[38]

Since, as was pointed out in the earlier discussion, such a finding has *already* been made in alternative contingent form by the Commission in its two opinions and formally embodied in its order of February 11, 1947, no purpose

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[37] Cf. R. 38, where the Court stated with respect to the contention that the redemption prices were the "equitable equivalent" of the rights surrendered by the preferred "* * * we do not believe that such a finding could be supported on the present record".

[38] If, on the other hand, the Circuit Court's language be construed paradoxically as a holding that the Commission may validly determine additional amounts to be payable to the preferred holders in this case, contrary to the determination of the District Court which the Circuit Court affirmed, such a ruling would imperatively call for consideration and determination by this Court of the respective statutory functions of the Commission and the District Court, as well as all those fundamental issues of "fairness and equity" under Section 11(e) which the Circuit Court held were correctly determined by the District Court.

would be served by the remand except to delay distribution to the common stockholders of the escrow fund and further protract the litigation of which the entire expense must be borne by the common stockholders (R. 72a-82a).

## CONCLUSION

For the reasons stated, this petition for a writ of certiorari to the Court of Appeals for the Third Circuit should be granted.

Dated: September 4, 1948.

Respectfully submitted,

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